1. Use the Mundell–Fleming model to predict what would happen to aggregate income, the exchange rate, and the trade balance under both floating and fixed exchange rates in response to each of the following shocks:
   a. A fall in consumer confidence about the future induces consumers to spend less and save more.
   b. The introduction of a stylish line of Toyotas makes some consumers prefer foreign cars over domestic cars.
   c. The introduction of automatic teller machines reduces the demand for money.

2. The Mundell–Fleming model takes the world interest rate $r^*$ as an exogenous variable. Let’s consider what happens when this variable changes.
   a. What might cause the world interest rate to rise?
   b. In the Mundell–Fleming model with a floating exchange rate, what happens to aggregate income, the exchange rate, and the trade balance when the world interest rate rises?
   c. In the Mundell–Fleming model with a fixed exchange rate, what happens to aggregate income, the exchange rate, and the trade balance when the world interest rate rises?

3. Business executives and policymakers are often concerned about the “competitiveness” of American industry (the ability of U.S. industries to sell their goods profitably in world markets).
   a. How would a change in the exchange rate affect competitiveness?
   b. Suppose you wanted to make domestic industries more competitive but did not want to alter aggregate income. According to the Mundell–Fleming model, what combination of monetary and fiscal policies should you pursue?